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## SECURITIES AND EXCHANGE COMMISSION

[Release No. 34-85798; File No. SR-BOX-2019-15]

### **Self-Regulatory Organizations; BOX Exchange LLC; Notice of Filing and Immediate Effectiveness of a Proposed Rule Change to Modify the Criteria for Listing an Option on an Underlying Covered Security**

May 7, 2019.

Pursuant to Section 19(b)(1) of the Securities Exchange Act of 1934 (“Act”),<sup>1</sup> and Rule 19b-4 thereunder,<sup>2</sup> notice is hereby given that on April 25, 2019, BOX Exchange LLC (“Exchange” or “BOX”) filed with the Securities and Exchange Commission (“Commission”) the proposed rule change as described in Items I and II below, which Items have been prepared by the self-regulatory organization. The Commission is publishing this notice to solicit comments on the proposed rule from interested persons.

#### **I. Self-Regulatory Organization’s Statement of the Terms of Substance of the Proposed Rule Change**

The Exchange proposes to amend BOX Rule 5020 (Criteria for Underlying Securities) to modify the criteria for listing an option on an underlying covered security. The text of the proposed rule change is available from the principal office of the Exchange, at the Commission’s Public Reference Room and also on the Exchange’s Internet website at <http://boxoptions.com>.

#### **II. Self-Regulatory Organization’s Statement of the Purpose of, and Statutory Basis for, the Proposed Rule Change**

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<sup>1</sup> 15 U.S.C. 78s(b)(1).

<sup>2</sup> 17 CFR 240.19b-4.

In its filing with the Commission, the self-regulatory organization included statements concerning the purpose of, and basis for, the proposed rule change and discussed any comments it received on the proposed rule change. The text of these statements may be examined at the places specified in Item IV below. The self-regulatory organization has prepared summaries, set forth in Sections A, B, and C below, of the most significant aspects of such statements.

A. Self-Regulatory Organization's Statement of the Purpose of, and Statutory Basis for, the Proposed Rule Change

1. Purpose

The Exchange proposes to amend BOX Rule 5020 (Criteria for Underlying Securities) to modify the criteria for listing an option on an underlying covered security. This is a competitive filing that is based on a proposal submitted by NASDAQ PHLX LLC ("Phlx") and approved by the Commission.<sup>3</sup> The Exchange proposes to modify Rule 5020(b)(5)(i) to permit the listing of an option on an underlying covered security that has a market price of at least \$3.00 for the previous three consecutive business days preceding the date on which the Exchange submits a certificate to the Options Clearing Corporation ("OCC") for listing and trading. The Exchange does not intend to amend any other criteria for listing options on an underlying security in Rule 5020.

Currently, the underlying covered security must have a closing market price of at least \$3.00 per share for the previous five consecutive business days preceding the date on which the Exchange submits a listing certificate to the OCC. In the proposed amendment, the market price will still be measured by the closing price reported in the primary market in which

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<sup>3</sup> See Securities Exchange Act Release No. 34-82474 (January 9, 2018) (Order Approving SR-Phlx-2017-75).

the underlying covered security is traded, but the measurement will be the price over the prior three consecutive business day period preceding the submission of the listing certificate to OCC, instead of the prior five business day period.

The Exchange acknowledges that the Options Listing Procedures Plan<sup>4</sup> requires that the listing certificate be provided to OCC no earlier than 12:01 a.m. and no later than 11:00 a.m. (Chicago time) on the trading day prior to the day on which trading is to begin.<sup>5</sup> The proposed amendment will still comport with that requirement. For example, if an initial public offering (“IPO”) occurs at 11 a.m. on Monday, the earliest date the Exchange could submit its listing certificate to OCC would be on Thursday by 12:01 a.m. (Chicago time), with the market price determined by the closing price over the three-day period from Monday through Wednesday. The option on the IPO would then be eligible for trading on the Exchange on Friday. The proposed amendment would essentially enable options trading within four business days of an IPO becoming available instead of six business days (five consecutive days plus the day the listing certificate is submitted to OCC).

At the time the Exchange adopted the “look back” period of five consecutive business days, it determined that the five-day period was sufficient to protect against attempts

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<sup>4</sup> The Plan for the Purpose of Developing and Implementing procedures Designed to Facilitate the Listing and Trading of Standardized Options Submitted Pursuant to Section 11a(2)(3)(B) of the Securities Exchange Act of 1934 (a/k/a the Options Listing Procedures Plan (“OLPP”)) is a national market system plan that, among other things, sets forth procedures governing the listing of new options series.

See Securities Exchange Act Release No. 44521 (July 6, 2001), 66 FR 36809 (July 13, 2001) (Order approving OLPP). The sponsors of OLPP include Phlx; OCC; BATS Exchange, Inc.; BOX Options Exchange LLC; C2 Options Exchange, Incorporated; Chicago Board Options Exchange, Incorporated; EDGX Exchange, Inc.; Miami International Securities Exchange, LLC; MIAx PEARL, LLC; The NASDAQ Stock Market LLC; NASDAQ BX, Inc.; Nasdaq GEMX, LLC; Nasdaq ISE, LLC; Nasdaq MRX, LLC; NYSE American, LLC; and NYSE Arca, Inc.

<sup>5</sup> See OLPP at page 3.

to manipulate the market price of the underlying security and would provide a reliable test for stability.<sup>6</sup> Surveillance technologies and procedures concerning manipulation have evolved since then to provide adequate prevention or detection of rule or securities law violations within the proposed time frame, and the Exchange represents that its existing trading surveillances are adequate to monitor the trading of options on the Exchange.<sup>7</sup>

Furthermore, the Exchange notes that the scope of its surveillance program also includes cross market surveillance for trading that is not just limited to the Exchange. In particular, the Financial Industry Regulatory Authority (“FINRA”), pursuant to a regulatory services agreement, operates a range of cross-market equity surveillance patterns on behalf of the Exchange to look for potential manipulative behavior, including spoofing, algorithm gaming, marking the close and open, and momentum ignition strategies, as well as more general, abusive behavior related to front running, wash shales, quoting/routing, and Reg SHO violations. These cross-market patterns incorporate relevant data from various markets beyond the Exchange, including data from the New York Stock Exchange (“NYSE”) and from the Nasdaq Stock Market (“Nasdaq”).

Additionally, for options, the Exchange, through FINRA, utilizes an array of patterns that monitor manipulation of options, or manipulation of equity securities (regardless

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<sup>6</sup> See Securities Exchange Act Release Nos. 47190 (January 15, 2003), 68 FR 3072 (January 22, 2003) (SR-CBOE-2002-62); 47352 (February 11, 2003), 68 FR 8319 (February 20, 2003) (SR-PCX-2003-06); 47483 (March 11, 2003), 68 FR 13352 (March 19, 2003) (SR-ISE-2003-04); 47613 (April 1, 2003), 68 FR 17120 (April 8, 2003) (SR-Amex-2003-19); and 47794 (May 5, 2003), 68 FR 25076 (May 9, 2003) (SR-Phlx-2003-27)

<sup>7</sup> Such surveillance procedures generally focus on detecting securities trading subject to opening price manipulation, closing price manipulation, layering, spoofing or other unlawful activity impacting an underlying security, the option, or both. The Exchange, through the Financial Industry Regulatory Authority (“FINRA”), has price movement alerts, unusual market activity and order book alerts active for all trading symbols. These real time patterns are active for the new security as soon as the IPO begins trading.

of venue) for the purpose of impacting options prices on BOX options facility (i.e., mini-manipulation strategies). Accordingly, the Exchange believes that the cross market surveillance performed by FINRA on behalf of the Exchange, coupled with the Exchange staff's real-time monitoring of similarly violative activity on the exchange as described herein, reflects a comprehensive surveillance program that is adequate to monitor for manipulation of the underlying security and overlying option within the proposed three-day look back period.

Furthermore, the Exchange notes that the proposed listing criteria would still require that the underlying security be listed on NYSE, the American Stock Exchange (now known as NYSE American), or the National Market System of The Nasdaq Stock Market (now known as the Nasdaq Global Market) (collectively, the "Named Markets"), as provided for in the definition of "covered security" from Section 18(b)(1)(A) of the 1933 Act.<sup>8</sup> Accordingly, the Exchange believes that the proposed rule change would still ensure that the underlying security meets the high listing standards of a Named Market, and would also ensure that the underlying is covered by the regulatory protections (including market surveillance, investigation and enforcement) offered by these exchanges for trading in covered securities conducted on their facilities.

Furthermore, according to Phlx's approved proposal, the Nasdaq, had no cases, within a five year period ending in 2018, where an IPO-related issue for which it had pricing information qualified for the \$3.00 price requirement during the first three (3) days of trading and did not qualify for the \$3.00 price requirement during the first five (5) days.<sup>9</sup> In other

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<sup>8</sup> See 15 U.S.C. 77r(b)(1)(A).

<sup>9</sup> There were over 750 IPO-related issues on Nasdaq within the past five years. Out of all of the issues with pricing information, there was only one issue that had a price below \$3.00 during the first five consecutive business days. The Exchange notes, however, that Nasdaq allows for companies to list on the Nasdaq Capital Market at \$2.00 or \$3.00 per

words, none of these qualifying issues fell below the \$3.00 threshold within the first three (3) or five (5) days of trading. As such, the Exchange believes that its existing surveillance technologies and procedures, coupled with Nasdaq's findings related to the IPO-related issues as described herein, adequately address potential concerns regarding possible manipulation or price stability within the proposed timeframe.

The Exchange also believes that the proposed look back period can be implemented in connection with the other initial listing criteria for underlying covered securities. In particular, the Exchange recognizes that it may be difficult to verify the number of shareholders in the days immediately following an IPO due to the fact that stock trades generally clear within two business days (T+2) of their trade date and therefore the shareholder count will generally not be known until T+2.<sup>10</sup> The Exchange notes that the current T+2 settlement cycle was recently reduced from T+3 on September 5, 2017 in connection with the Commission's amendments to Exchange Rule 15c6-1(a) to adopt the shortened settlement cycle,<sup>11</sup> and the look back period of three (3) consecutive business days proposed herein reflects this shortened T+2 settlement period. As proposed, stock trades would clear within T+2 of their trade date (i.e., within three (3) business days) and therefore the number of shareholders could be verified within three (3) business days, thereby enabling options trading within four (4) business days of

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share in some instances, which was the case for this particular issue. See Nasdaq Rule 5500 Series for initial listing standards on the Nasdaq Capital Market. See also supra note 3.

<sup>10</sup> The number of shareholders of record can be validated by large clearing agencies such as the Depository Trust and Clearing Corporation ("DTCC") upon the settlement date (i.e., T+2).

<sup>11</sup> See Securities Exchange Act Release no. 78962 (September 28, 2016), 81 FR 69240 (October 5, 2016) (Amendment to Securities Transaction Settlement Cycle) (File No. S7-22-16).

an IPO (three (3) consecutive business days plus the day the listing certificate is submitted to OCC).

Furthermore, the Exchange notes that various brokerage firms that have a large retail customer clientele can confirm the number of individual customers who have a position in new issues. The earliest that these firms can provide confirmation is usually the day after the first day of trading (T+1) on an unsettled basis, while others can confirm on the third day of trading (T+2). For the foregoing reasons, the Exchange believes that basing the proposed three (3) business day look back period on the T+2 settlement cycle would allow for sufficient verification of the number of shareholders.

The proposed rule change will apply to all covered securities that meet the criteria of Rule 5020. Pursuant to Rule 5020, the Exchange establishes guidelines to be considered in evaluating the potential underlying securities for Exchange option transactions.<sup>12</sup> However, the fact that a particular security may meet the guidelines established by the Exchange does not necessarily mean that it will be approved as an underlying security.<sup>13</sup> As part of the established criteria, the issuer must be in compliance with any applicable requirement of the Securities Exchange Act of 1934.<sup>14</sup> Additionally, in considering the underlying security, the Exchange relies on information made publicly available by the issuer and/or the markets in which the security is traded.<sup>15</sup> Even if the proposed option meets the objective criteria, the Exchange may decide not to list, or place limitations or conditions upon listing.<sup>16</sup> The Exchange believes that

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<sup>12</sup> See Exchange Rule 5020. The Exchange established specific criteria to be considered in evaluating potential underlying securities for Exchange option transactions.

<sup>13</sup> Id.

<sup>14</sup> See Exchange Rule 5020(b)(3).

<sup>15</sup> See Exchange Rule 5020(d).

<sup>16</sup> See Exchange Rule 5020(b).

these measures, together with its existing surveillance procedures, provide adequate safeguards in the review of any covered security that may meet the proposed criteria for consideration of the option within the timeframe contained in this proposal.

## 2. Statutory Basis

The Exchange believes that the proposal is consistent with the requirements of Section 6(b) of the Securities Exchange Act of 1934 (the “Act”),<sup>17</sup> in general, and Section 6(b)(5) of the Act,<sup>18</sup> in particular, in that it is designed to prevent fraudulent and manipulative acts and practices, to promote just and equitable principles of trade, to foster cooperation and coordination with persons engaged in facilitating transactions in securities, to remove impediments to and perfect the mechanism of a free and open market and a national market system, and, in general to protect investors and the public interest.

In particular, the Exchange believes that the proposed changes to its listing standards for covered securities would allow the Exchange to more quickly list options on a qualifying covered security that has met the \$3.00 eligibility price without sacrificing investor protection. As discussed above, the Exchange believes that its existing trading surveillances provide a sufficient measure of protection against potential price manipulation within the proposed three (3) consecutive business day timeframe. The Exchange also believes that the proposed three (3) consecutive business day timeframe would continue to be a reliable test for price stability in light of Nasdaq’s findings that none of the IPO-related issues on Nasdaq, within a five year time period ending in 2018, qualified for the \$3.00 per share price standard during the first three trading days fell below the \$3.00 threshold during the fourth or fifth trading day.

Furthermore, the established guidelines to be considered by the Exchange in evaluating the

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<sup>17</sup> 15 U.S.C. 78f(b).

<sup>18</sup> 15 U.S.C. 78f(b)(5).



potential underlying securities for Exchange option transactions,<sup>19</sup> together with existing trading surveillances, provide adequate safeguards in the review of any covered security that may meet the proposed criteria for consideration of the option within the proposed timeframe.

In addition, the Exchange believes that basing the proposed timeframe on the T+2 settlement cycle adequately addresses the potential difficulties in confirming the number of shareholders of the underlying covered security. For the foregoing reasons, the Exchange believes that the proposed amendments will remove impediments and perfect the mechanism of a free and open market and a national market system by providing an avenue for investors to swiftly hedge their investment in the stock in a shorter amount of time than what is currently in place.<sup>20</sup>

Finally, it should be noted that a price/time standard for the underlying security was first adopted when the listed options market was in its infancy, and was intended to prevent the proliferation of options being listed on low-priced securities that presented special manipulation concerns and/or lacked liquidity needed to maintain fair and orderly markets.<sup>21</sup> When options trading commenced in 1973, the Commission determined that it was necessary for securities underlying options to meet certain minimum standards regarding both the quality of the issuer and the quality of the market for a particular security.<sup>22</sup> These standards, including a price/time standard, were imposed to ensure that those issuers upon whose

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<sup>19</sup> See notes 12-16 above.

<sup>20</sup> This proposed rule change does not alter any obligations of issuers or other investors of an IPO that may be subject to a lock-up or other restrictions on trading related securities.

<sup>21</sup> See Securities Exchange Act Release No. 29628 (August 29, 1991), 56 FR 43949-01 (September 5, 1991) (SR-AMEX-86-21; SR-CBOE-86-15; SR-NYSE-86-20; SR-PSE86-15; and SR-PHLX-86-21) (“1991 Approval Order”) at 43949 (discussing the Commission’s concerns when options trading initially commenced in 1973).

<sup>22</sup> See 1991 Approval Order at 43949.

securities options were to be traded were widely-held, financially sound companies whose shares had trading volume and float substantial enough so as not to be readily susceptible to manipulation.<sup>23</sup> At the time, the Commission determined that the imposition of these standards was reasonable in view of the pilot nature of options trading and the limited experience of investors with options trading.<sup>24</sup>

Now more than 40 years later, the listed options market has evolved into a mature market with sophisticated investors. In view of this evolution, the Commission has approved various exchange proposals to relax some of these initial listing standards throughout the years,<sup>25</sup> including reducing the price/time standard in 2003 from \$7.50 per share for the majority of business days over a three month period to the current \$3.00 per share/five business day standard (“2003 Proposal”).<sup>26</sup> It has been over sixteen years since the Commission approved the 2003 proposal, and both the listed options market and exchange technologies have continued to evolve since then. In this instance, the Exchange is only proposing a modest reduction of the current five (5) business day standard to three (3) business days to correspond to the securities industry’s move to a T+2 standard settlement cycle.<sup>27</sup> The \$3.00 per share standard and all other initial options listing criteria in Rule 5020 will remain unchanged by this proposal. For the reasons discussed herein, the Exchange therefore

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<sup>23</sup> Id.

<sup>24</sup> Id.

<sup>25</sup> See e.g., 1991 Approval Order (modifying a number of initial listing criteria, including the reduction of the price/time standard from \$10 per share each day during the preceding three calendar months to \$7.50 per share for the majority of days during the same period).

<sup>26</sup> See Securities Exchange Act Release Nos. 47190 (January 15, 2003), 68 FR 3072 (January 22, 2003) (SR-CBOE-2002-62); 47352 (February 11, 2003), 68 FR 8319 (February 20, 2003) (SR-PCX-2003-06); 47483 (March 11, 2003), 68 FR 13352 (March 19, 2003) (SR-ISE-2003-04); 47613 (April 1, 2003), 68 FR 17120 (April 8, 2003) (SRAmex-2003-19); and 47794 (May 5, 2003), 68 FR 25076 (May 9, 2003) (SR-Phlx-200327).

<sup>27</sup> See supra note 11.

believes that the proposed three (3) business day period will be beneficial to the marketplace without sacrificing investor protections.

B. Self-Regulatory Organization's Statement on Burden on Competition

The Exchange does not believe that the proposed rule change will impose any burden on competition not necessary or appropriate in furtherance of the purposes of the Act. In this regard and as indicated above, the Exchange notes that the rule change is being proposed as a competitive response to a filing submitted by Phlx that was approved by the Commission.<sup>28</sup> The proposed rule change will reduce the number of days to list options on an underlying security, and is intended to bring new options listings to the marketplace quicker.

C. Self-Regulatory Organization's Statement on Comments on the Proposed Rule Change Received from Members, Participants, or Others

The Exchange has neither solicited nor received comments on the proposed rule change.

III. Date of Effectiveness of the Proposed Rule Change and Timing for Commission Action

Because the foregoing proposed rule change does not: (i) significantly affect the protection of investors or the public interest; (ii) impose any significant burden on competition; and (iii) become operative for 30 days from the date on which it was filed, or such shorter time as the Commission may designate, it has become effective pursuant to Section 19(b)(3)(A)(iii) of the Act<sup>29</sup> and subparagraph (f)(6) of Rule 19b-4 thereunder.<sup>30</sup>

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<sup>28</sup> See supra, note 3.

<sup>29</sup> 15 U.S.C. 78s(b)(3)(A)(iii).

<sup>30</sup> 17 CFR 240.19b-4(f)(6). In addition, Rule 19b-4(f)(6)(iii) requires a self-regulatory organization to give the Commission written notice of its intent to file the proposed rule change, along with a brief description and the text of the proposed rule change, at least five business days prior to the date of filing of the proposed rule change, or such shorter time as designated by the Commission. The Exchange has satisfied this requirement.

A proposed rule change filed under Rule 19b-4(f)(6)<sup>31</sup> normally does not become operative prior to 30 days after the date of the filing. However, Rule 19b-4(f)(6)(iii)<sup>32</sup> permits the Commission to designate a shorter time if such action is consistent with the protection of investors and the public interest. The Exchange has asked the Commission to waive the 30-day operative delay so that the proposal may become operative immediately upon filing. The Exchange states that the waiver of the operative delay will ensure fair competition among the exchanges by allowing the Exchange to modify the criteria for listing an option on an underlying covered security which is currently allowed on other options exchanges. The Commission believes that waiver of the 30-day operative delay is consistent with the protection of investors and the public interest. Accordingly, the Commission hereby waives the operative delay and designates the proposed rule change as operative upon filing.<sup>33</sup>

At any time within 60 days of the filing of the proposed rule change, the Commission summarily may temporarily suspend such rule change if it appears to the Commission that such action is: (i) necessary or appropriate in the public interest; (ii) for the protection of investors; or (iii) otherwise in furtherance of the purposes of the Act. If the Commission takes such action, the Commission shall institute proceedings to determine whether the proposed rule should be approved or disapproved.

#### IV. Solicitation of Comments

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<sup>31</sup> 17 CFR 240.19b-4(f)(6).

<sup>32</sup> 17 CFR 240.19b-4(f)(6)(iii).

<sup>33</sup> For purposes only of waiving the 30-day operative delay, the Commission has also considered the proposed rule's impact on efficiency, competition, and capital formation. See 15 U.S.C. 78c(f).

Interested persons are invited to submit written data, views, and arguments concerning the foregoing, including whether the proposed rule change is consistent with the Act. Comments may be submitted by any of the following methods:

Electronic Comments:

- Use the Commission's Internet comment form (<http://www.sec.gov/rules/sro.shtml>);
- or
- Send an e-mail to [rule-comments@sec.gov](mailto:rule-comments@sec.gov). Please include File Number SR-BOX-2019-15 on the subject line.

Paper Comments:

- Send paper comments in triplicate to Secretary, Securities and Exchange Commission, 100 F Street, NE, Washington, DC 20549-1090.

All submissions should refer to File Number SR-BOX-2019-15. This file number should be included on the subject line if e-mail is used. To help the Commission process and review your comments more efficiently, please use only one method. The Commission will post all comments on the Commission's Internet website (<http://www.sec.gov/rules/sro.shtml>). Copies of the submission, all subsequent amendments, all written statements with respect to the proposed rule change that are filed with the Commission, and all written communications relating to the proposed rule change between the Commission and any person, other than those that may be withheld from the public in accordance with the provisions of 5 U.S.C. 552, will be available for website viewing and printing in the Commission's Public Reference Room, 100 F Street, NE, Washington, DC 20549, on official business days between the hours of 10:00 a.m. and 3:00 p.m. Copies of the filing also will be available for inspection and copying at the

principal office of the Exchange. All comments received will be posted without change.

Persons submitting comments are cautioned that we do not redact or edit personal identifying information from comment submissions. You should submit only information that you wish to make available publicly. All submissions should refer to File Number SR-BOX-2019-15 and should be submitted on or before **[INSERT DATE 21 DAYS FROM PUBLICATION IN THE *FEDERAL REGISTER*]**.

For the Commission, by the Division of Trading and Markets, pursuant to delegated authority.<sup>34</sup>

**Eduardo A. Aleman,**

*Deputy Secretary.*

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<sup>34</sup> 17 CFR 200.30-3(a)(12).

